LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS
200 W. Washington, Suite 301
Indianapolis, IN 46204
(317) 233-0696
http://www.in.gov/legislative

FISCAL IMPACT STATEMENT

LS 6448 | **NOTE PREPARED:** Jan 1, 2014
BILL NUMBER: HB 1124 | **BILL AMENDED:**

SUBJECT: Local Income Tax Laws.

FIRST AUTHOR: Rep. Thompson | **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: X **GENERAL** | **IMPACT:** State & Local
DEDICATED
FEDERAL

Summary of Legislation: This bill replaces the County Adjusted Gross Income Tax (CAGIT), the County Option Income Tax (COIT), and the County Economic Development Income Tax (CEDIT) with a local income tax law.

The bill also provides for the introduction of legislation in the 2015 legislative session to make related amendments to implement the Local Income Tax (LIT).

Effective Date: Upon passage; January 1, 2015.

Explanation of State Expenditures: *Summary-* The bill requires the Department of Local Government Finance, the Department of State Revenue, and the State Budget Agency to perform certain tasks throughout 2014 in preparation for the conversion on January 1, 2015. The bill's requirements are within the agencies' routine administrative functions and should be able to be implemented with no additional appropriations, assuming near customary agency staffing and resource levels.

Additional Information- Department of Local Government Finance (DLGF): The DLGF is required to recalculate maximum permissible levies. They are required to eliminate the effect of levy freezes and other levy reductions related to CAGIT, COIT, and CEDIT. This is necessary in order to provide a uniform method of calculating levies, tax rates, and application of the property tax credits established by the bill. The DLGF is also charged with assisting the adopting bodies as necessary to transition to the LIT.

Department of State Revenue (DOR): The DOR will incur additional expenses to revise tax forms, instructions, and computer programs to transition to the new tax. The DOR's current level of resources should be sufficient to implement these provisions.

State Budget Agency (SBA): The SBA is required to work with the DLGF to adjust county tax rates to eliminate any additional revenue that would be collected once the LIT rate is imposed on taxpayers. The bill moves the deadline for the determination of supplemental distributions from November 1 to October 1. Otherwise, the certified distribution process is identical to current law.

Explanation of State Revenues:

Summary of NET Local Impact: This bill repeals CAGIT, COIT, CEDIT, LOIT to Freeze Property Tax Levies, LOIT for Property Tax Relief, and LOIT for Public Safety and replaces them with a single Local Income Tax (LIT) effective January 1, 2015. Notwithstanding transition errors, the implementation of LIT should not result in a net fiscal impact on county income tax revenue. A county should continue to receive the revenue it is currently receiving unless it adopts, increases, decreases, or rescinds a tax rate. Generally, revenue would be used for the same or similar purposes as under the current LOITs.

Explanation of Local Expenditures: The adopting bodies will remain the same for each county that currently imposes a LOIT. The process to adopt, decrease, increase, and rescind the tax rates also remains the same. The adopting bodies should have sufficient resources to the implement the LIT.

Explanation of Local Revenues: *Summary -* The bill repeals CAGIT, COIT, CEDIT, and the optional rate components: LOIT to Freeze Property Tax Levies, LOIT for Property Tax Relief, and LOIT for Public Safety. It replaces those taxes with one Local Income Tax (LIT). In most cases, the total LOIT rate will remain the same as the counties transition to the new tax. However, the maximum LIT rate authorized by the bill would be higher than for the current taxes.

The bill imposes the tax on resident and nonresident county taxpayers equally, so nonresident county taxpayers will be taxed at a higher rate than under current statute. This would affect only non-Indiana residents working in Indiana. However, the SBA may reduce the overall tax rate to make the transition revenue neutral, so the rates for resident county taxpayers may decrease slightly.

Additional Information - The bill establishes one local income tax comprised of elements from CAGIT, COIT, and CEDIT. The procedures to alter the rates remain the same. The rates may only be changed through an ordinance by the adopting body. The rate effective dates are the same except if an ordinance was adopted after October 31 of the current year and before January 1 of the immediately succeeding year, the rate takes effect on October 1 of the immediately succeeding year. While the LIT is one tax, it is has three separate rate components: the expenditure rate, the property tax relief rate, and the restricted purpose rate.

The *expenditure rate* revenue is dedicated for public safety, economic development, and certified shares. This rate may not exceed 1.25%. This is equal to both the combined COIT, CEDIT, and LOIT for Public Safety rate, and the combined CEDIT, LOIT for Public Safety, and the portion of CAGIT not dedicated for property tax relief. The revenue collected from this rate may be used for the purposes described in the bill. The methods of allocating certified shares is identical to current law.

The tax collected from the *property tax relief rate* is to be treated as property taxes for all purposes except by the DLGF in computing maximum levy limits. The tax may be used only to fund a property tax credit to reduce property tax liabilities. This rate replaces the LOIT for Property Tax Relief, LOIT to Freeze Property Tax Levies, the CEDIT rate for Homestead Credits, and the property tax relief portion of CAGIT. The rate may not exceed 2.5%.

Restricted purpose rates are distinct rates implemented for a specific purpose by a particular county. For example, Union County may impose a restricted rate of up to 0.25% in addition to all other rates for the sole purpose of renovating their county courthouse. The most common use of restricted purpose rates are to fund the construction and operation of correctional facilities. The tax collected from this rate must be deposited in a separate account, and sufficient records must be maintained to demonstrate the revenue is used only for the designated purpose. These rates can vary depending on the project. However, not all county-specific tax rates are found in this section. If the revenue from a restricted purpose rate is used to reduce property taxes in order to fund a special project, then the rate is classified as an additional property tax relief rate.

Excluding restricted purpose tax rates, all counties have a maximum potential LIT rate of 3.75%. Under current law, the maximum rate for a county may vary between 3.25% and 3.50%, with some specific rate exceptions. The determination of the maximum LOIT rate depends on the county and which LOIT rates a county has adopted. In addition, CAGIT and COIT have separate nonresident county taxpayer rates, while CEDIT has one rate for all county taxpayers. The LIT rate is imposed equally on all county taxpayers.

While the transition to the new tax in January 2015 should have little impact on most taxpayers, once the LIT is in place, the counties will have additional flexibility on how they use the tax revenue. For example, under current law, the maximum levy freeze LOIT (up to 1%) and the portion of legacy CAGIT that reduces property tax levies (up to 0.25%) are effectively property tax credits applied to all property at a uniform rate. The LOIT for Property Tax Relief (up to 1%) can be allocated to (1) homesteads, (2) residential property, (3) other real and personal property, or (4) any combination of the three. The CEDIT homestead / residential credits (up to 0.25%) can be allocated to both homesteads and other residential property.

So, out of the 2.5% maximum tax rate, 1.25% benefits all property, 0.25% benefits homesteads and/or residential property, and the remaining 1% can be allocated to any property types.

This bill would give counties more flexibility in the future over how property tax credits are allocated. Counties would be able to allocate credits in any combination among homesteads subject to the 1% cap, qualified residential and other property subject to the 2% cap, or real and personal property subject to the 3% cap.

Also, under current law, a county that allocates credits to qualified residential property applies those credits to nonhomestead residential property as well as to homestead property. Under this bill, a county could decide to allocate credits to 2% cap properties including nonhomestead residential, without being required to apply credits to homesteads.

All future fiscal impacts would depend on local decisions.

State Agencies Affected: Department of Local Government Finance; Department of State Revenue; State Budget Agency.

Local Agencies Affected: Counties that impose a local option income tax.

Information Sources:

Fiscal Analyst: Heath Holloway, 232-9867; Bob Sigalow 232-9859.